

# Newly Minted Rules for Deducting Performance Compensation under Section 162(m)

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The Internal Revenue Service ("IRS") recently issued Revenue Ruling 2008-13, which restricts payments that will be considered as performance compensation under section 162(m) for purposes of the \$1 million limit on a deduction for compensation paid to executives of publicly traded companies. If certain requirements are met, the rules under 162(m) except performance pay from the \$1 million limit.

The recent revenue ruling presents a narrow interpretation of the regulations under section 162(m) and concludes that compensation paid under an arrangement for performance compensation is not entitled to the exception as performance compensation if the compensation is also payable after termination without cause, termination for good reason or voluntary retirement. In other words, if the compensation is payable under these broad circumstances, the IRS will not recognize such compensation as performance pay under section 162(m) even though a particular payment may be in fact based on performance.

The regulations under 162(m) provide that performance compensation is excepted from the deduction limitation if it meets specified requirements and is payable solely on account of the attainment of a specified performance goals. The regulations also permit arrangements for performance pay programs to offer payment upon death, disability or change in control without losing the benefit of the exception.

The new ruling will not apply for performance periods beginning on or before January 1, 2009 or for compensation paid pursuant to employment contracts in effect on February 21, 2008 (excluding renewals, either automatic or by agreement).

Companies will now have to review their performance pay programs to restrict payment triggers to the attainment of specified performance goals, upon death disability or change in control. Companies that want to permit certain terminated executives to continue to benefit from participation in the performance pay program should consider amending such programs to provide for payment only after attainment of the performance goals even though the executive has terminated or some permissible pro-ration of the performance pay based on attainment of performance goals as of the date of termination. Companies should also review any employment agreements with performance pay provisions to assess any automatic renewals and when the new rules will apply.

**If you have any additional questions, please contact:**



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